

POWER PROGRAM

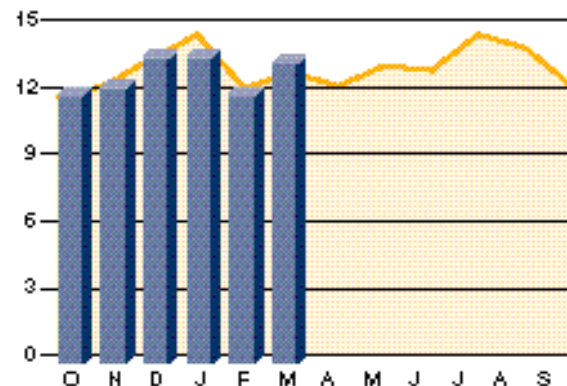
# Second Quarter Report

1998



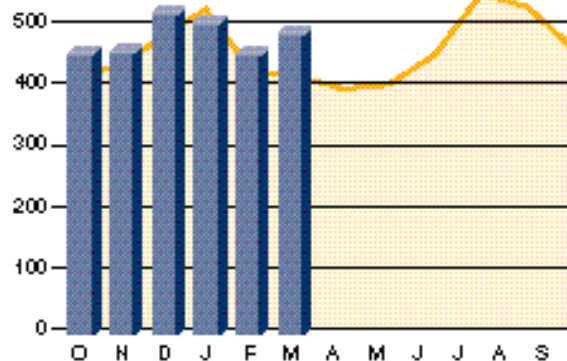
## Total TVA Generation

billions of kwh



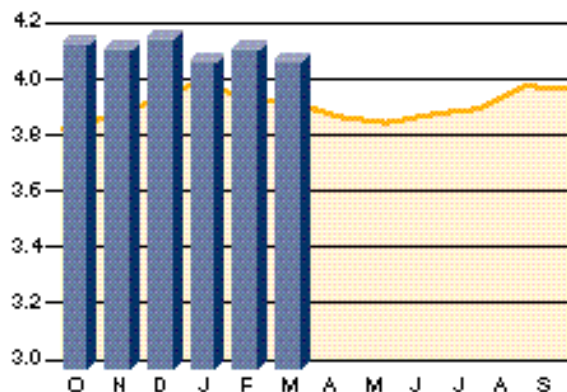
## Total Electric Revenue

millions of dollars



## Average Revenue

cents per kwh



Tennessee Valley Authority  
400 West Summit Hill Drive  
Knoxville, Tennessee 37902-1499  
6M 4/98

Fiscal Year 1998  
 Fiscal Year 1997

During the second quarter, TVA continued to meet the challenges of increased competition through our accomplishments in maintaining operational excellence, enhancing our financial position, and serving our customers and the public interest.

Net income for the six months ending March 31, 1998, was \$44 million, an improvement of \$114 million over the same period last year. This was due to growth in energy sales of about three percent, along with additional revenues from the rate increase implemented in October 1997.

In January, Watts Bar Nuclear Plant received superior ratings in three of four areas assessed by the Nuclear Regulatory Commission, placing it among the highest-performing nuclear plants in the country. In February, all five TVA nuclear units operated continuously for 100 days or more, saving TVA about \$13 million over projections. And in March, Browns Ferry Unit 3 surpassed 365 continuous days online, setting the record for the longest continuous operation by a large TVA generator.

We recently appointed Mr. Oswald "Ike" Zeringue to a newly created position of President and Chief Operating Officer, giving him responsibility for TVA's power production, transmission and resource stewardship functions. We also consolidated all TVA-wide financial functions under the Chief Financial Officer to ensure greater independence and consistency in the financial review and analysis of all aspects of TVA's business. Both of these actions were taken as part of TVA's continuing efforts to prepare for success in the restructured utility industry.

Two Wall Street firms gave TVA high marks in recently-issued reports. The report by Merrill Lynch stated, "TVA is facing the future head on and is taking steps to improve its competitive position.

TVA will be a major force in the electric marketplace... once competition is fully implemented." And the report by Salomon Smith Barney says, "... [We are] impressed with the ongoing story of this unique triple-A rated utility...we believe that the business plan in place at TVA...is one that will be increasingly viewed in a positive way by investors."

TVA welcomes the move to a more competitive marketplace. We will continue to focus on providing financial flexibility, operational excellence, and superior service to our customers.

Sincerely,



Craven Crowell

#### Financial Highlights (millions)

Six Months Ended March 31	1998	1997
Operating revenues	\$ 2,942	\$ 2,714
Operating expenses	(1,965)	(1,781)
Operating income	977	933
Other income, net	55	1
Interest expense	(988)	(1,004)
<b>Net income (loss)</b>	<b>\$ 44</b>	<b>\$ (70)</b>

#### Sales of Electricity (millions - kWh)

Six Months Ended March 31	1998	1997
Municipalities and cooperatives	57,858	55,700
Industries directly served	9,153	8,359
Federal agencies	3,437	4,365
<b>Total sales of electricity</b>	<b>70,448</b>	<b>68,424</b>

## RESULTS OF OPERATIONS

Net income for the second quarter of 1998 amounted to \$59 million, an improvement of \$65 million from the net loss of \$6 million for the second quarter of 1997. Net income for the six months ended March 31, 1998, amounted to \$44 million, an improvement of \$114 million from the net loss of \$70 million for the same period last year.

### Operating Revenues

Operating revenues for the three months ended March 31, 1998, were \$1,477 million compared with \$1,382 million for the same period last year. The \$95 million increase was primarily due to a rate increase effective October 1, 1997, coupled with an increase in energy sales of approximately 1 billion kilowatt-hours (3 percent) as a result of colder weather compared with the second quarter of 1997. Fiscal year-to-date operating revenues increased \$228 million from \$2,714 million in 1997 to \$2,942 million in 1998. This year-to-date increase is also attributable to the rate increase implemented for 1998, as well as an increase in kilowatt-hour sales of 3 percent from 68 billion kilowatt-hours in 1997 to 70 billion kilowatt-hours in 1998.

### Operating Expenses

Operating expenses increased \$69 million from \$886 million for the three months ended March 31, 1997, to \$955 million for the same period of 1998. This increase is primarily attributable to higher fuel and purchased power costs as a result of higher overall generation, higher coal prices, and lower hydro generation. Operating expenses for the six months ended March 31, 1998, were \$1,965 million compared with \$1,781 million for the same period last year. The \$184 million increase consists primarily of higher net fuel and purchased power expense related to higher overall generation and higher coal prices, higher depreciation and amortization expenses related to capital project completions, and higher general and administrative expenses as a result of an accounting change (such costs are no longer allocated partially to capital projects, but instead are expensed in the period incurred).

### Interest Expense

Net interest expense decreased \$10 million and \$16 million for the three months and six months ended March 31, 1998, respectively, compared with the same periods of 1997. These reductions result from both a lower level of total outstanding debt and lower average interest rates during 1998.

## FINANCIAL POSITION

Net cash provided by operations increased \$63 million and \$16 million for the three months and six months ended March 31, 1998, respectively, compared with the same periods of 1997. Cash used for construction activities declined \$40 million and \$91 million for the three months and six months ended March 31, 1998, respectively, compared with the same periods of 1997. These reductions reflect the continued emphasis on cost control and process improvement initiatives. Operating cash flow, net of cash used for construction activities, was \$312 million for the six months to date and will be applied toward TVA's debt reduction efforts.

## BALANCE SHEETS *(Unaudited)*

	March 31 1998	September 30 1997
(MILLIONS)		
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 643	\$ 299
Accounts receivable	593	701
Inventories (at average cost) and other		
Fuel	151	112
Other	314	287
Total current assets	<b>1,701</b>	1,399
<b>Property, plant, and equipment</b>		
Completed plant	28,704	28,528
Less accumulated depreciation	(7,537)	(7,178)
Net completed plant	21,167	21,350
Construction in progress	565	605
Deferred nuclear generating units	6,306	6,303
Nuclear fuel and capital lease assets	938	1,040
Total property, plant, and equipment	<b>28,976</b>	29,298
<b>Investment funds</b>	<b>643</b>	561
<b>Deferred charges and other assets</b>		
Loans and other long-term receivables	124	121
Debt issue and reacquisition costs	806	1,096
Other deferred charges	1,566	1,209
Total deferred charges and other assets	<b>2,496</b>	2,426
<b>Total assets</b>	<b><u>\$33,816</u></b>	<u>\$ 33,684</u>
<b>LIABILITIES AND PROPRIETARY CAPITAL</b>		
<b>Current liabilities</b>		
Accounts payable	\$ 354	\$ 468
Accrued liabilities	126	161
Accrued interest	499	499
Discount notes	1,717	2,151
Current maturities of long-term debt	203	574
Total current liabilities	<b>2,899</b>	3,853
<b>Other liabilities</b>	<b>2,197</b>	1,704
<b>Long-term debt</b>		
Public bonds—senior	20,999	20,354
Federal Financing Bank—senior	3,200	3,200
Public bonds—subordinated	1,100	1,100
Unamortized discount and other	(568)	(502)
Total long-term debt	<b>24,731</b>	24,152
<b>Proprietary capital</b>		
Appropriation investment	578	588
Retained earnings reinvested in power program	3,411	3,387
Total proprietary capital	<b>3,989</b>	3,975
<b>Total liabilities and proprietary capital</b>	<b><u>\$33,816</u></b>	<u>\$ 33,684</u>

## STATEMENTS OF INCOME *(Unaudited)*

	Three Months Ended March 31		Six Months Ended March 31	
	1998	1997	1998	1997
	(MILLIONS)		(MILLIONS)	
<b>Operating revenues</b>				
Sales of electricity				
Municipalities and cooperatives	\$ 1,290	\$ 1,204	\$ 2,580	\$ 2,350
Industries directly served	115	110	242	227
Federal agencies	55	46	86	97
Other	17	22	34	40
Total operating revenues	<u><b>1,477</b></u>	<u>1,382</u>	<u><b>2,942</b></u>	<u>2,714</u>
<b>Operating expenses</b>				
Fuel and purchased power, net	314	273	643	555
Operating and maintenance	317	301	674	603
Depreciation and amortization	259	244	517	488
Tax-equivalents	65	68	131	135
Total operating expenses	<u><b>955</b></u>	<u>886</u>	<u><b>1,965</b></u>	<u>1,781</u>
<b>Operating income</b>	<b>522</b>	496	<b>977</b>	933
Other income (expense), net	<u>28</u>	<u>(1)</u>	<u>55</u>	<u>1</u>
Income before interest charges	<u><b>550</b></u>	<u>495</u>	<u><b>1,032</b></u>	<u>934</u>
<b>Interest expense</b>				
Interest on debt	483	498	977	997
Amortization of debt discount, issue, and reacquisition costs, net	21	25	40	49
Allowance for funds used during construction	<u>(13)</u>	<u>(22)</u>	<u>(29)</u>	<u>(42)</u>
Net interest expense	<u><b>491</b></u>	<u>501</u>	<u><b>988</b></u>	<u>1,004</u>
<b>Net income (loss)</b>	<u><b>\$ 59</b></u>	<u>\$ (6)</u>	<u><b>\$ 44</b></u>	<u>\$ (70)</u>

## STATEMENTS OF CASH FLOWS *(Unaudited)*

<b>Cash flows from operating activities</b>				
Net income (loss)	\$ 59	\$ (6)	\$ 44	\$ (70)
Items not requiring cash	329	300	646	601
Other changes, net	93	124	(132)	11
Net cash provided by operations	<u><b>481</b></u>	<u>418</u>	<u><b>558</b></u>	<u>542</u>
<b>Cash flows from investing activities</b>				
Construction expenditures	(123)	(163)	(240)	(331)
Allowance for funds used during construction	13	22	29	42
Other, net	<u>(9)</u>	<u>(6)</u>	<u>(35)</u>	<u>(41)</u>
Net cash used in investing activities	<u><b>(119)</b></u>	<u>(147)</u>	<u><b>(246)</b></u>	<u>(330)</u>
<b>Cash flows from financing activities</b>				
Borrowings, net	(560)	(251)	(163)	(395)
Other	<u>(103)</u>	<u>(18)</u>	<u>195</u>	<u>(33)</u>
Net cash (used in) provided by financing activities	<u><b>(663)</b></u>	<u>(269)</u>	<u><b>32</b></u>	<u>(428)</u>
<b>Net change in cash and cash equivalents</b>	<u><b>\$ (301)</b></u>	<u>\$ 2</u>	<u><b>\$ 344</b></u>	<u>\$ (216)</u>